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The FOOD MARKETING INDUSTRY SPEAKS 1984

Published by:

The Research Division
Food Marketing Institute
1750 K Street, NW
Washington, DC 20006

Price:

Food Marketing Industry Speaks, 1984
FMI Members: $7.50
Nonmembers: $15.00

Food Marketing Industry Speaks, 1984 and
Detailed Tabulations from the Food Marketing
Industry Speaks, 1984
FMI Members: $15.00
Nonmembers: $30.00

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The Food Marketing Institute (FMI) is a non-profit association that conducts programs in research, education and public affairs on behalf of its 1,300 members—food retailers and wholesalers and their customers in the United States and overseas. FMI's domestic member companies operate over 17,000 retail food stores with a combined annual sales volume of $130 billion—half of all grocery sales in the United States. More than three-fourths of FMI's membership is comprised of independent supermarket operators or small regional firms. Its international membership includes more than 100 members from 40 nations.

The FOOD MARKETING INDUSTRY SPEAKS.

The United States economy continued its vigorous recovery in 1983. Many factors contributed to this positive outlook. It was the third straight year of substantially reduced inflation; the Consumer Price Index rose by only 3.2 percent, the lowest 12-month increase since 1964. While inflation declined, the Gross National Product rose 3.3 percent. But probably the best news was the decline in unemployment. The year's decrease of 2.2 percentage points in unemployment meant that more than four million Americans went back to work between January and December of 1983.

Economic factors have also had a positive affect on the supermarket industry. Although retail and wholesale sales increases showed a continuation of their downward trend, after being adjusted for inflation, the 1983 figures showed increases in both retail and wholesale sales. In addition, the gross profit margin for both companies with warehouses and companies without warehouses rose again in 1983.

This report examines all the interdependent parts of our industry that work together to put food on the dinner tables of America: the food producer, the manufacturer, the wholesaler, and the retailer. It begins with a review of the economy in general with an in-depth look at those aspects which affect our industry directly. It covers sales and profit trends, and provides a detailed look at several special interest areas.

Highlighted this year, for example are distribution centers—both wholesale and retail, for dry grocery and refrigerated foods centers. The report also examines in detail the produce department, electronic funds transfer, medical benefit programs, and productivity by store type.

Much of the data are compiled through FMI's annual surveys of the industry. FMI gratefully acknowledges all those companies who gave their time and effort to fill out the questionnaires. A detailed explanation of the study is provided in the appendix.

Industry information is also drawn from other FMI research reports such as *Operations Review* and *Facts About Store Development*. The Institute would also like to acknowledge data gathered from *Forbes Magazine*, the U.S. Departments of Agriculture and Commerce, and many other business and government publications.

While this report contains the complete analysis for 1983, it does not include the cross tabulations of survey data from which this analysis was developed. This information, providing a more thorough look at industry activity, is contained in a separate, supplemental report entitled *Detailed Tabulations* from the *Food Marketing Industry Speaks, 1984*. Another publication, *Trends—Consumer Attitudes and the Supermarket, 1984*, parallels *Speaks* by presenting the state of the industry from the consumer side. *Trends* explores consumer attitudes toward the economy and the supermarket, and analyzes changes in consumer concerns and shopping patterns.

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IN 1983

Retail Sales Gain Over Previous Year	7.6%
Wholesale Sales Gain Over Previous Year	4.1%
Weekly Sales Per Square Foot	$6.90
Sale Per Customer Transaction	$14.60
Sales Per Labor Hour	$91.00
Gross Margin With Warehouse	23.7%
Gross Margin Without Warehouse	21.5%
Net Profit (before taxes)	1.3%
Weekly Store Sales	$153,600

These operating results are typical of FMI's member supermarkets. They represent average performance based on data from a cross-section of our membership.

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The ECONOMIC SETTING

Economic Growth

The Food Distribution industry, like every other industry, functions in the broad context of the nationwide economic environment. To fully understand this industry, one must view it in the context of trends in American life.

In 1983, the U.S. economy recovered vigorously. In fact, 1983 was so good that in 10, 20 or 30 years from now when people reminisce about the "Good Ole Days," they may well be talking about 1983.

1983 was the third straight year of substantially reduced inflation. The economy experienced double-digit inflation in 1980 and 1981, but only six percent in '82; and then less than four percent in 1983. During 1983, consumer prices rose by only 3.2 percent and producer prices by 0.6 percent. To put this in perspective, this rise in consumer prices was the smallest since 1972. For producer prices, it was the lowest 12-month increase since 1964. While inflation declined, the Gross National Product (GNP) rose 3.3 percent. In terms of real dollars, this represents a growth of almost $50 billion over the 1982 level.

Perhaps the best news on the economic front lies in the area of unemployment. Our highest monthly unemployment rate in 1983 was 10.4 percent of the civilian workforce. This figure is down from the high of 10.7 percent in 1982.

However, because most unemployment is of relatively short duration, unemployment touched a much larger number of our households than this percentage would indicate. In fact, at sometime during the calendar year 1982, almost 25 percent of all households had at least one wage earner unemployed.

The steady monthly decline in unemployment from January to December 1983 shows that the trend is reversing. The year's decrease of 2.2 percentage points in unemployment means that more than four million Americans have gone back to work since January.

In addition to these gains in employment and declines in inflation, both productivity and real wages rose, continuing an advance that began in 1982.

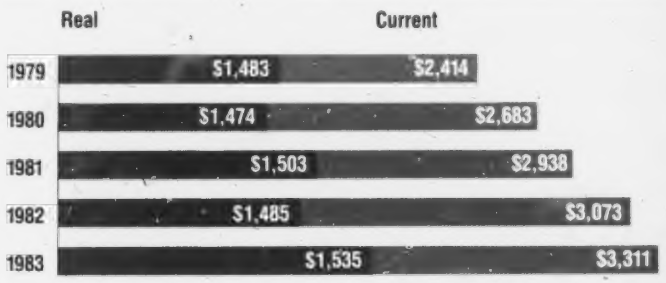
The major stock markets rose through the first half of the year then leveled off while the U.S. dollar appreciated in the foreign exchange markets, continuing a trend that began in late 1980. One result of the strong dollar is a higher price abroad for U.S. exports. This creates a lower demand for U.S. products and has weakened the U.S. economy for the last three years.

Even with a growing balance of payments deficit, the domestic economy has been very good news for both homebuilders and home buyers. In 1983, housing starts were in the neighborhood of 1.7 million and sales of single-family homes increased by about 52 percent over 1982 levels. The housing industry also benefited from a year of relatively low and stable interest rates. Perhaps the key word is stable. Although 1983 rates were low compared to the recent past, they were still high by historical standards. However, the fact that rates were less volatile than in recent years helped restore confidence to financial markets, to investors, and to consumers. Consumers have adjusted to these higher rates faster than economists believed they could.

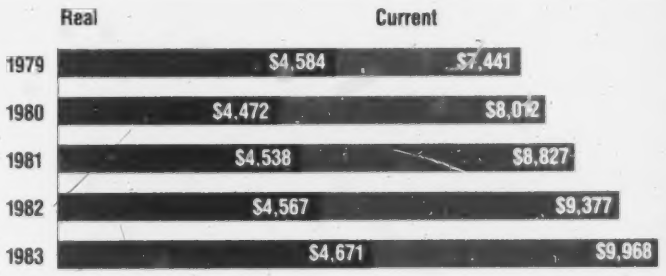
The economy has remained strong right through the first quarter of 1984 prompting fears of a new surge in inflation. An unusual pattern of recovery may mean that the old rules may not apply.

Not since the year 1940 has the U.S. entered the second year of a recovery with over eight percent

Gross National Product (Billions)



Per Capita Disposable Income



unemployment and under 80 percent of our manufacturing capacity utilized. Because of this, wage increases are likely to remain moderate and production bottlenecks few and far between. Barring any unforseen supply shocks, a major renewal of accelerating inflation may not occur this year.

What does this mean to consumers? The real meaning can be stated quite simply: more consumers had more money in their pockets than in any year in recent history. This shows up best in per capita disposable income. In terms of current dollars, the average American now has almost $600 more in disposable income than in 1982.

Although FMI does not collect data on restaurant sales, the Department of Commerce does. By examining restaurant sales an even greater insight is gained into the effects of economic growth on consumers.

Restaurant sales increases were high during the first part of 1983, but slacked off toward the end of the year. The two year trend shows that restaurant sales, in essence, peaked in late 1982 and early 1983. When people begin to feel the budget squeeze, one of their first reactions is to eat away from home less; when they see things improving, they begin to eat out a little more.

Food Production

The 1983 drought and acreage reductions reduced stocks and boosted prices of grains and other crops. Additionally, the outbreak of the avian flu among chickens and turkeys in the east and in California has meant that many, many flocks have been destroyed and that several areas have been quarantined. The flu's greatest impact, however, has been on egg production.

Grain producers recognized the Department of Agriculture's Payment-In-Kind (PIK) program as one of the most generous income transfer programs they had been offered in the 50-year history of federal farm programs. Farmers signed up in large numbers and as a result, participation in acreage reduction programs increased significantly in 1983. Then complications set in. Record acreage reductions occurred precisely in the same year as cold weather, floods, and droughts of historic proportions. All of this had a tremendous impact on crop production—particularly on the grain crops.

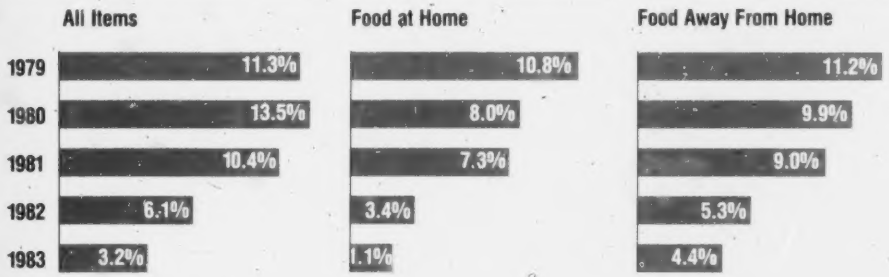
For example, corn production was at its lowest level in five years —almost half of what it was in 1982. This is reflected not only in the number of acres planted, but also in the number of acres harvested and in bushels per acre. Consequently, the price per bushel increased roughly 20 percent.

The same held true for wheat production which decreased by 387 million bushels from 1982 levels. Production of fresh fruit and fresh vegetables also declined, but this was due more to the weather conditions than to acreage reduction programs. The bitter cold experienced by most sections of the country around Christmas damaged citrus crops from Texas to Florida and even damaged the trees themselves. Some winter vegetable acreage was totally destroyed.

On the other side of the coin, beef, pork, and milk production all increased over their 1982 levels as did poultry. However, poultry production had been affected recently by the outbreak of the avian flu.

The loss of fruit and vegetable crops which resulted from December's cold spell were expected to be partially offset by increased imports. For example, Brazil exported frozen concentrated orange juice to help alleviate the 17 percent drop in U.S. citrus production and in late 1983 Mexico shipped extra vegetables.

Consumer Price Index



Sales Increase Over '82 By Quarters

The INDUSTRY

Wholesaling

Sales increases for food wholesalers averaged 4.1 percent in 1983 down from six percent in 1982. The interesting aspect of this, however, is that after adjustments for inflation, real sales increases were up over 1982 to three percent. This represents a prime example of the positive effect declining inflation has had on the food distribution industry. Additionally, the average sales for a retail store served by a wholesaler increased to $2.18 million in 1983.

Of the numerous and varied services wholesalers provided to their membership in 1983, more than 90 percent offered handling of private label stock and individual retail pricing. More than 80 percent provided product movement data, handling of generic labels, advertising, equipment procurement, and gross margin reports by item.

Retailing

On the retail side, 1983 sales increased 7.6 percent, continuing a five year trend in declining sales increases. As with wholesale increases, however, real sales increases for retailers were up, rising to 6.4 percent after being adjusted for inflation. The past two years are good examples of the benefits from controlling inflation.

This very favorable increase as compared to the recent past reflects two forces at work. First, over the early 1980s inflation was so high that virtually all of the yearly sales gains disappeared when we deflated the numbers. In 1983 inflation was brought under control. Second, in the late 1970s and early 1980s some very large companies in the industry were experiencing substantial problems. Many of these companies have now stabilized or actually accomplished a turnaround. Others have left the industry.

This impact is quite evident when identical store sales are compared to total store sales. Identical store sales in current dollars demonstrated the lowest annual increase in six years at 6.1 percent. But again, this increase, although appearing low, was greater than the inflation rate and resulted in real sales increases of 4.9 percent, the highest in six years.

Forbes Magazine's annual study of industry profitability will help put this into perspective. Stockholders' equity (net worth), which reflects the earning power of the stockholders' equity, decreased slightly from last year's 16.9 percent to 16.2 percent in 1983.

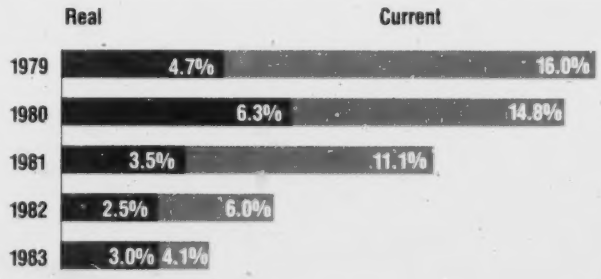
Forbes defines return on stockholders' equity as the percentage return on the stockholders' portion of a company's capital. Forbes calculates this by taking earnings per common share as a percentage of stockholders' equity per share at the start of the year. It is assumed that all convertible preferred stocks have been converted, which explains why this figure may be lower than others.

Return on total capital (total assets), which measures the ability of the industry's assets to generate profits, was also down slightly from last year's five-year high of 10.7 percent—registering this year at 10.5 percent, still higher than for any of the four years prior to 1982.

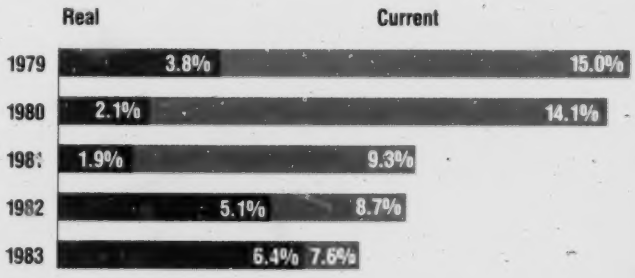
Return on total capital, calculated by *Forbes*, is the percentage return on a combination of stockholders' equity (both common and preferred) and long-term debt, including current maturities, minority stockholders' equity in consolidated subsidiaries, accumulated deferred taxes and investment tax credits. The profit figure for this calculation includes tax income, minority interest in net income and estimated after tax interest paid on long-term debt.

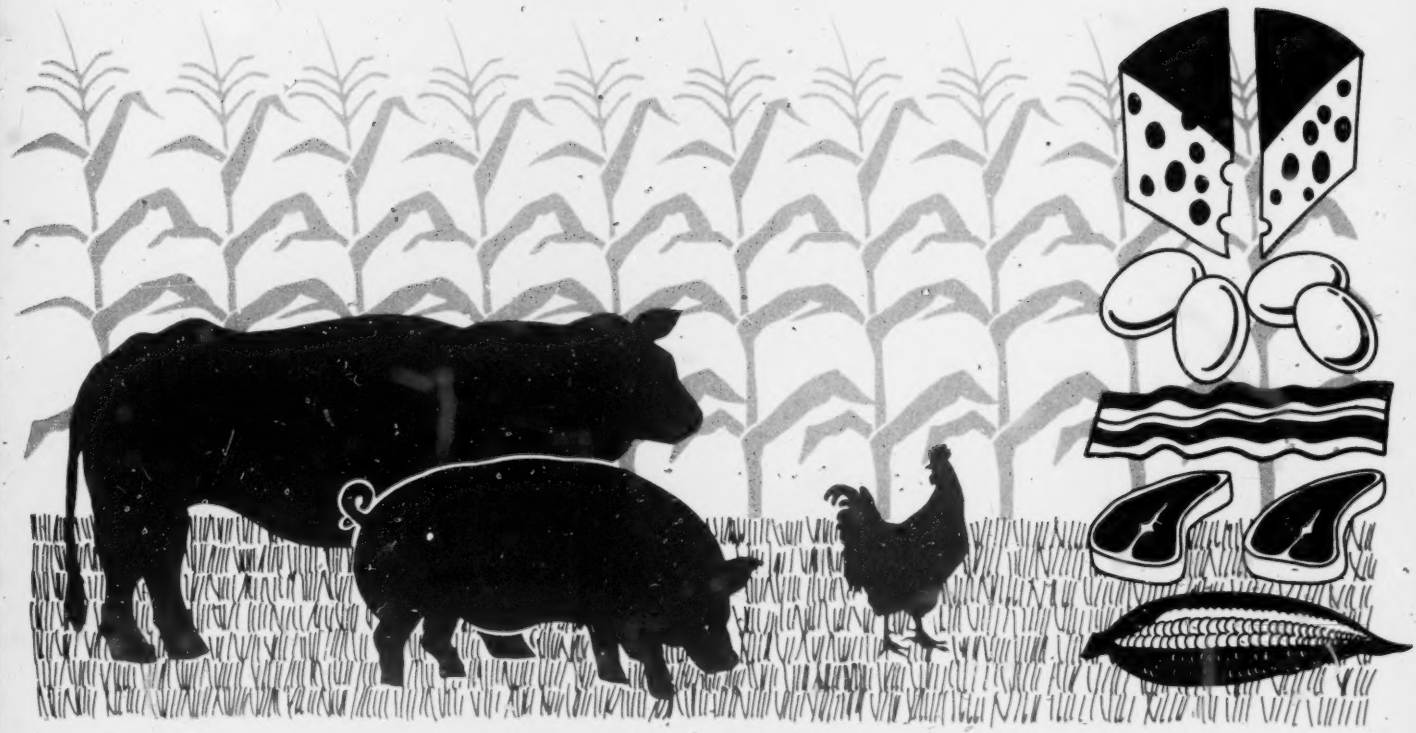
Membership Services Provided by Wholesalers	
Individual Retail Pricing	96%
Handle Private Label	98%
Advertising Programs	88%
Handle Generic Label	90%
Product Movement Data	90%
Equipment Procurement	82%
Gross Margin Report by Item	82%
Retail Accounting	74%
Member Payroll	65%
Real Estate & Store Engineering	76%
Education/Training	69%
Equipment & Fixture Financing	57%
Interior Decor & Design Service	65%
Scanning Support	59%
Discount Program	65%
Space Allocation	49%
Lease Financing	53%
DSD System	55%

Wholesale Sales Increase

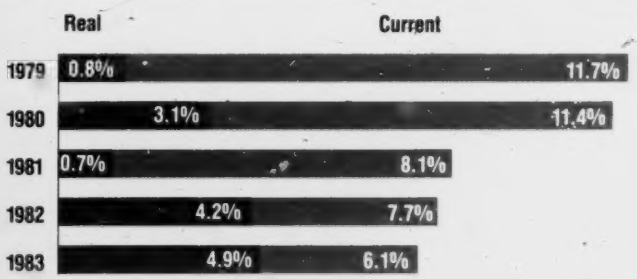


Retail Sales Increase

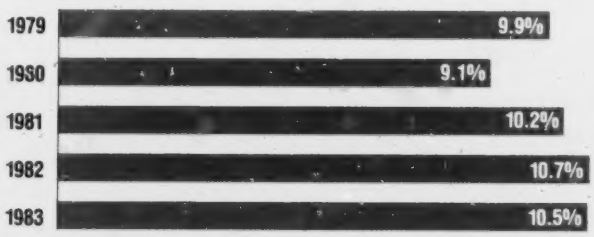




Identical Store Sales Increase

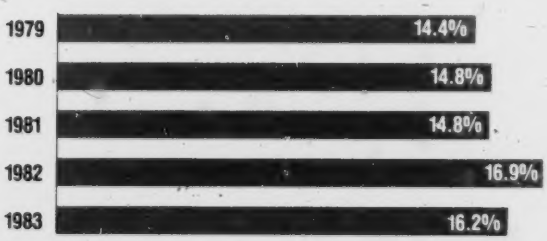


Return On Total Assets*



*Source *Forbes*

Return on Net Worth*



*Source *Forbes*

COMPANY PERFORMANCE

Gross Profit Margin

Gross profit margin represents total sales income minus the cost of goods sold. All expenses and profits come out of the gross profit margin. For companies without their own warehouse, the gross profit margin was 21.5 percent. Companies with their own warehouse saw a margin of 23.7 percent.

Store door margin, which represents gross margin minus warehouse and delivery costs, increased to 19.4 percent, slightly higher than the 1982 margin of 19.2 percent.

Net Profit Margin

Net profit margin, which is calculated by dividing net profits by net sales, decreased from 1.5 percent in 1982 to 1.3 percent in 1983. Quarterly net profits showed that the second and third quarters were the most profitable for 1983.

Productivity

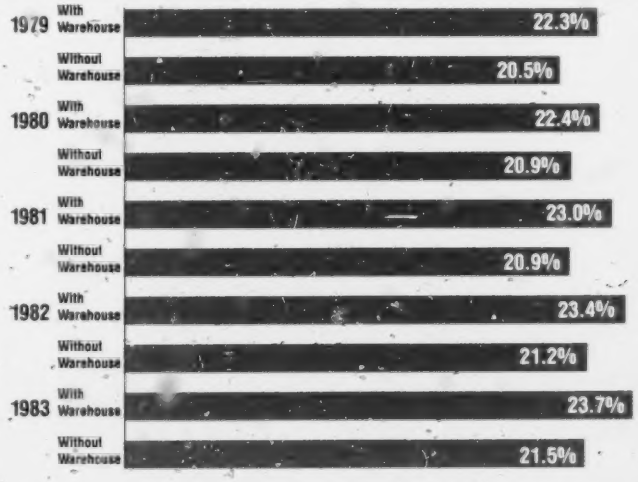
Another factor which helps determine profitability is productivity. FMI research found that in 1983 average weekly supermarket sales were $153,600. Combination stores recorded the highest average weekly sales at $291,230. They were followed by warehouse stores at $202,330 and super stores at $186,200. Conventional stores were the only type which recorded weekly sales less than the industry average. They averaged $100,000 per week.

Sale per customer transaction was $14.60 compared to $14.33 last year. In terms of real dollars, however, they were the lowest since 1980. Warehouse stores led in average sales per customer transaction with $22.15; followed by super stores and combination stores. Again, only conventional stores, with an average sale per customer transaction of $14.02, fell below the industry average.

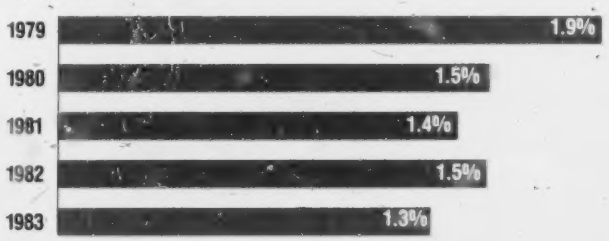
Sales per square foot of selling area decreased over last year, both in terms of current dollars—from $7.90 to $6.95—and in terms of real dollars—from $2.83 to $2.37. As would be expected, warehouse stores led in sales per square foot with $8.00, followed by conventional stores, combination stores, and super stores.

Sales per labor hour followed the trend of the last three years increasing slightly in current dollars, but decreasing in terms of real dollars. Warehouse stores demonstrated the highest sales per labor hour with $130.80. Super stores were next with $91.00, which equaled the in-

Gross Profit Margin



Net Profit Margin before taxes



dustry average, followed by conventional stores at $88.20 and combination stores at $87.00.

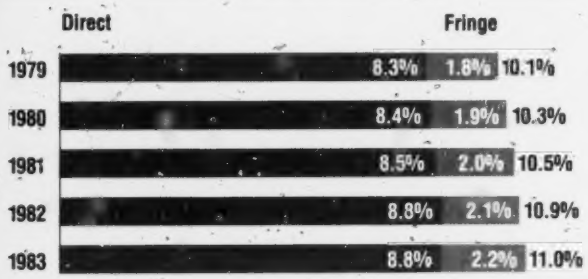
The typical supermarket in 1983 contained 28,000 square feet in total area. Combination stores averaged 45,875 square feet, followed by super stores, warehouse stores, and conventional stores. Combination stores also carried the largest number of items, averaging 25,000 and had the highest average retail price per item at $1.55. Warehouse stores averaged the lowest retail price per item, $1.18. The lowest average number of items carried were by warehouse stores with 9,000 items, although many of the super warehouse stores will carry up to 15,000 items.

Larger retailers, and particularly chains, relied on their own warehouses for over half of their products—56.6 percent. However, in 1983, almost one-fourth of all products arrived at stores via direct vendor deliveries. Independents relied more heavily on direct vendor deliveries than did chains, 33 percent to 25.7 percent.

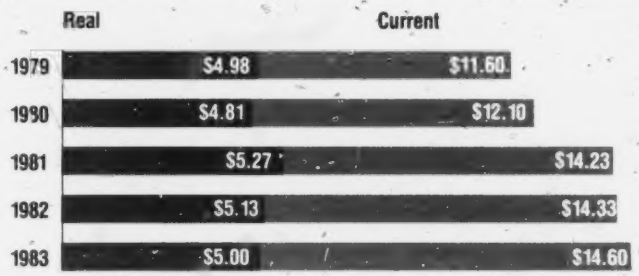
Percentage of Operation Supplied by

	All Companies	*Larger Retailer*	*Independent*
Own Warehouse	51%	57%	5%
Voluntary Wholesaler	11%	11%	9%
Cooperative Wholesaler	8%	3%	47%
Unaffiliated Wholesaler	4%	4%	7%
Direct Vendor Deliveries	27%	57%	33%

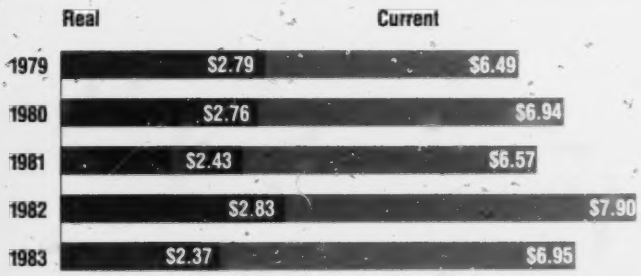
Total Store Labor Cost



Sale Per Transaction



Sales Per Square Foot



Sales Per Labor Hour